Rick Bensignor's

IN THE KNOW TRADER

Positioning Individual Investors Alongside Professionals

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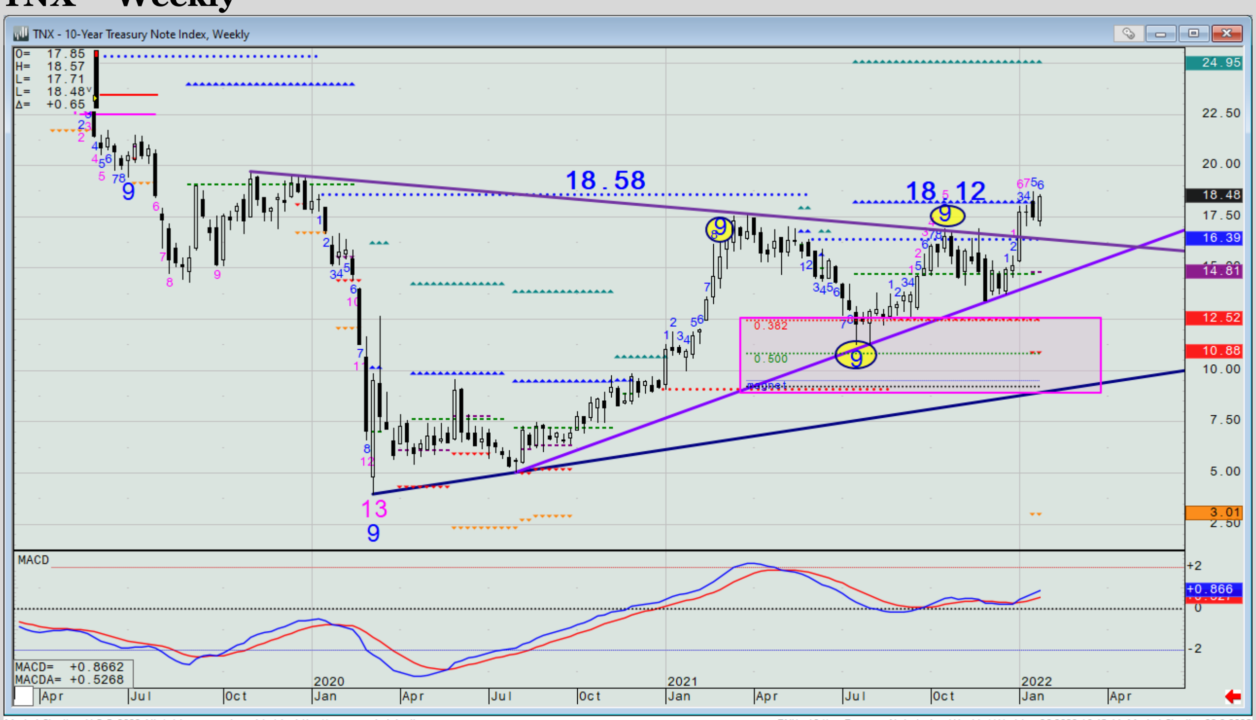
TACTICAL TRADER REPORT

The Macro Picture

A lot of the fluff has been taken out of risk asset prices in January, as investors finally face the reality that the Fed-fueled free money environment of the past dozen years is coming to an end. It took no time at all to see stocks drop sharply and interest rates rally in the past week, and then Fed Chairman Powell's press conference showed a perfect example of how fast a large gain day could disappear in minutes.

From an equity market point of view, the long-term picture is still bullish, with the correction halting its current decline just near the top of the SPX weekly cloud. It's the near- and medium-term picture that is more unclear, as the breach of 4518 was clearly meaningful, and it won't be a piece of cake for the market to materially get past that now on reflex rallies. For benchmark US 10-yr. interest rates, they have yet to break above my key 1.86% resistance level, so despite the inverted head-and-shoulders pattern having broken above its neckline, those positioned for that yield upmove have yet to see it materialize – but they're certainly getting closer.

TNX – Weekly

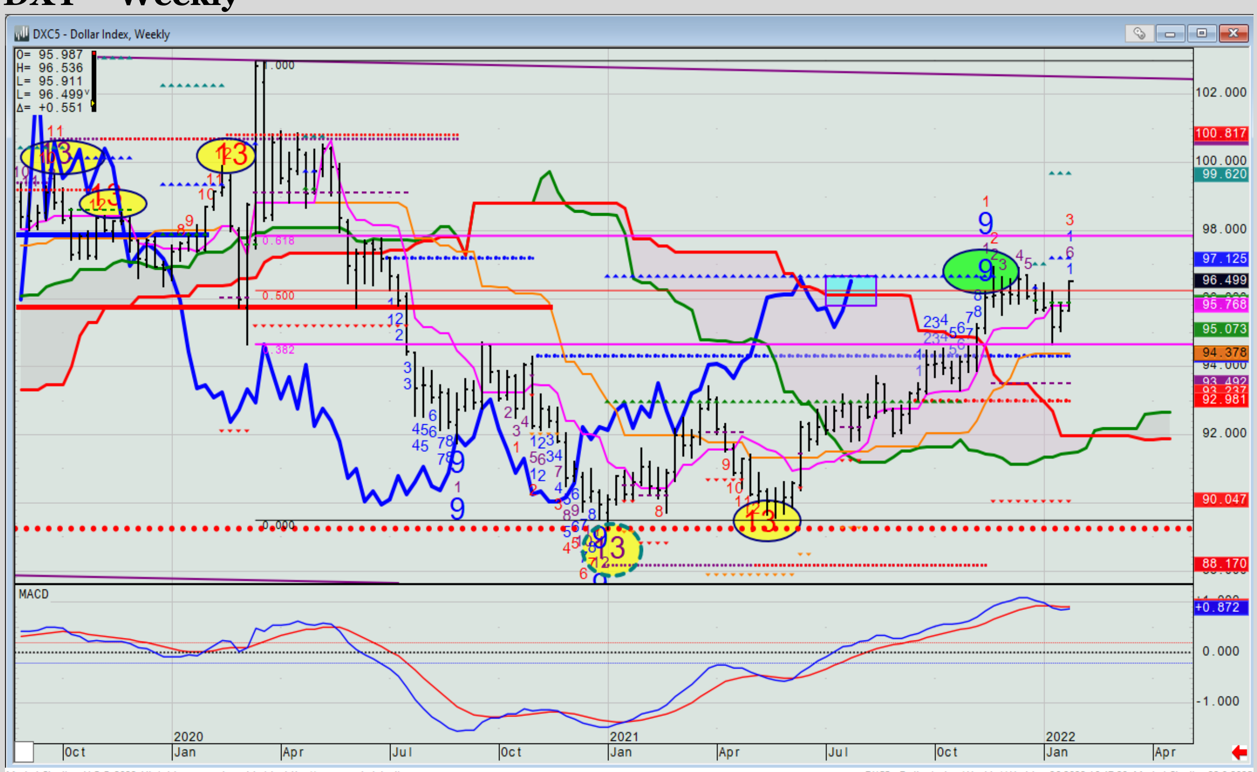


The bottoming pattern does measure to 3.25%, but in the more medium-term view, I do have Propulsion targets at 2.25 to 2.5 percent, and I believe they'll be achieved this year.

Let’s look at the always needed to be watched **ICE BofA Corporate Index Option-Adjusted Credit Spread**. It has now closed above 1.04% for two days in a row with Monday and Tuesday both seeing 1.05% readings. I’m still in the camp that a move that stays above 1.04% will likely take the spread up to test 1.34% to 1.46%. A move like that – though still hugely lower than the 4.01% peak it hit in March 2020 – would be a headwind to stock rallies holding gains.

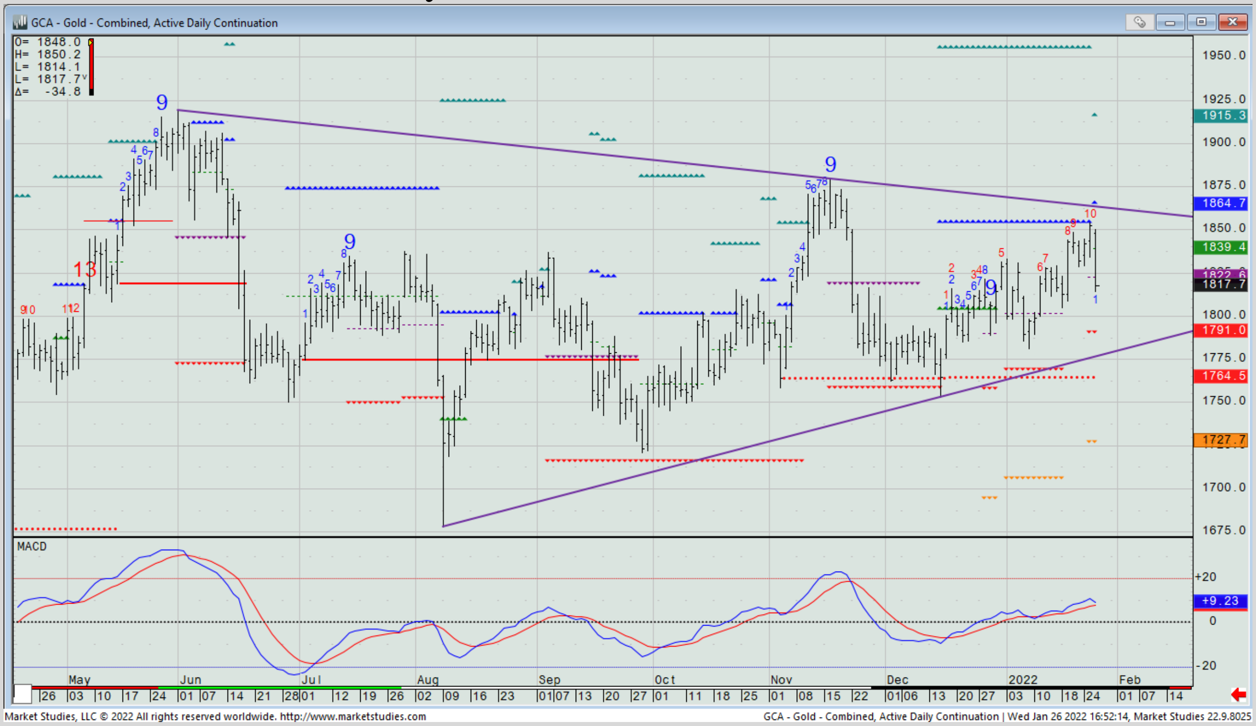
The US Dollar is breaking out as the cloud’s Lagging Line (in bold blue) has broken above the top of its cloud. (See the cyan-colored box.) Though price has not yet taken out recent highs, this should all but remove the major technical reasons to be leaning bearishly. If these gains hold up through week’s end, then the DXY probably heads higher to the 98 level – which would *not* be welcome by precious metals holders.

DXY – Weekly



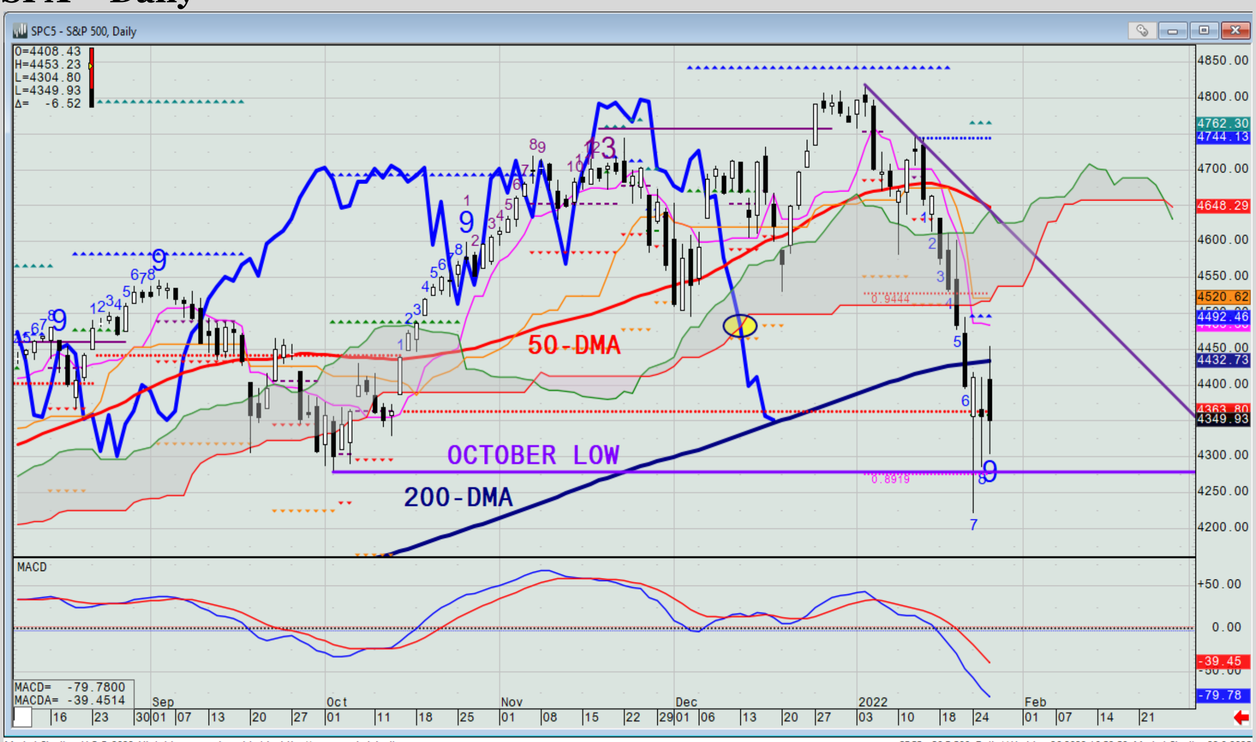
Gold remains in a medium-term sideways pattern and lacks any real trend (other than having no directional trend).

Gold Futures –Active Daily Continuation

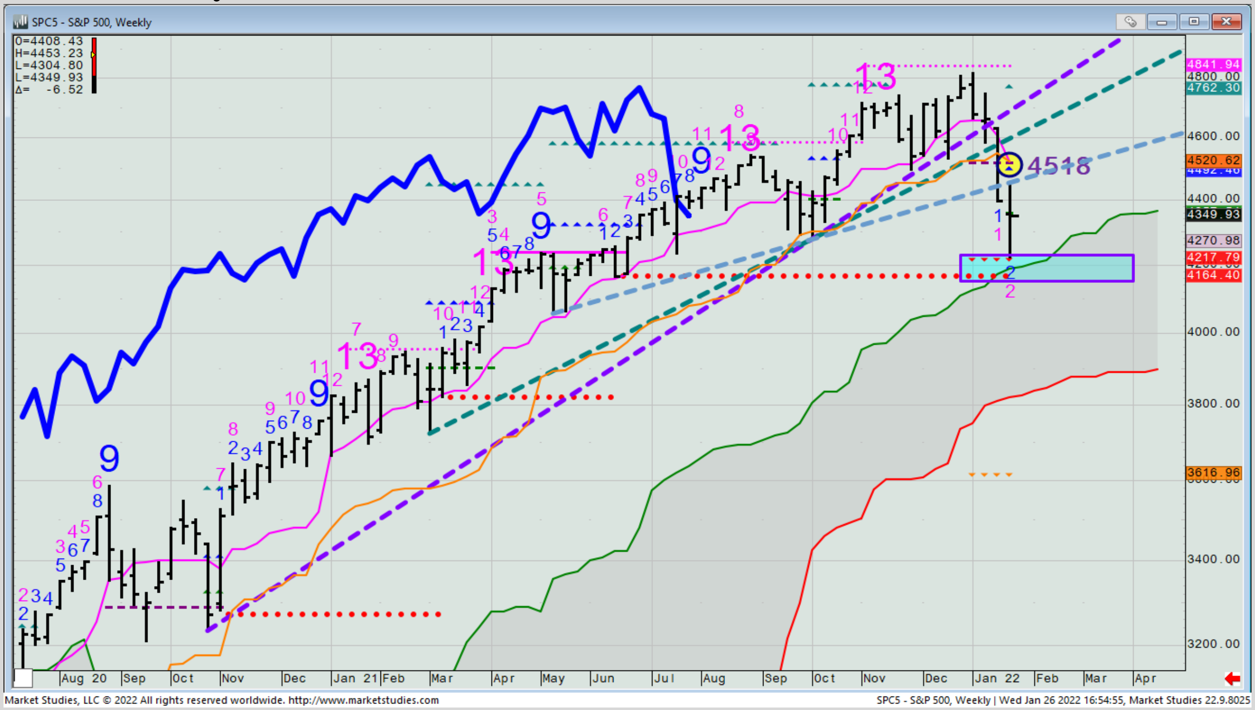


Our call for a breaking of SPX 4518 would lead to a test of the 4218—4164 zone was a good one with Monday's low at 4222. As I mentioned in this week's show on Stockcharts, success in life is about being prepared, and it's certainly so in the markets. Our having been able to identify where the game would change was defined well in advance of the market getting there, and it should have helped you reduce your equity exposure before things sold off another 5% into Monday's low.

SPX – Daily



SPX – Weekly



Last week I mentioned that this week would be very volatile, and Mr. Market did not disappoint us. Intraday moves are huge, and we've seen a couple of 100-pt. SPX swings in hours. To wit, in the first week of January, the 10-DMA of the SPX's daily range was 45 points. It's now 105 points per day!

So, it's very easy to do a double-take of your quote board, not quite believing you're seeing what you are. This will likely persist for some more time, which is also why you need to cut your trade position sizing in *half*.

Lastly, there is a case to believe we'll be in a two-way trading market for weeks to come, certainly until things calm down. I expect I'll be selling rallies to the 4475—4525 zone, using that opportunity to clean out names in my portfolios that I simply don't need to still own.

THIS WEEK'S NEW TRADE IDEA

It appears as if the credit spread we watch is breaking out, and with an expected subsequent 30 to 40 basis point upside target, let's put this idea of widening credit spreads to use. One of the easiest ways to do this is to buy a Treasury bond ETF and sell an investment grade bond ETF against it in a pair trade – the very essence of playing the credit spread.

Let's buy **the iShares 7-10 Year Treasury Bond ETF (IEF) and short the iShares Investment Grade Bond ETF (LQD)** against it. This pair will make money if the yield spread widen between the two instruments. We will use the aforementioned ICE BofA spread as the benchmark to time our trading of this pair. So once we get in this pair trade today, we will look to exit it into the ICE BofA 1.34% to 1.46% range – something we can more finely tune when we get closer to that target. We will also stop ourselves out on a couple of days in a row that the ICE BofA spread closes beneath 95 bps. – it's recent pullback low before the breakout. (See chart top of page 5.)

Long IEF vs. Short LQD – Weekly

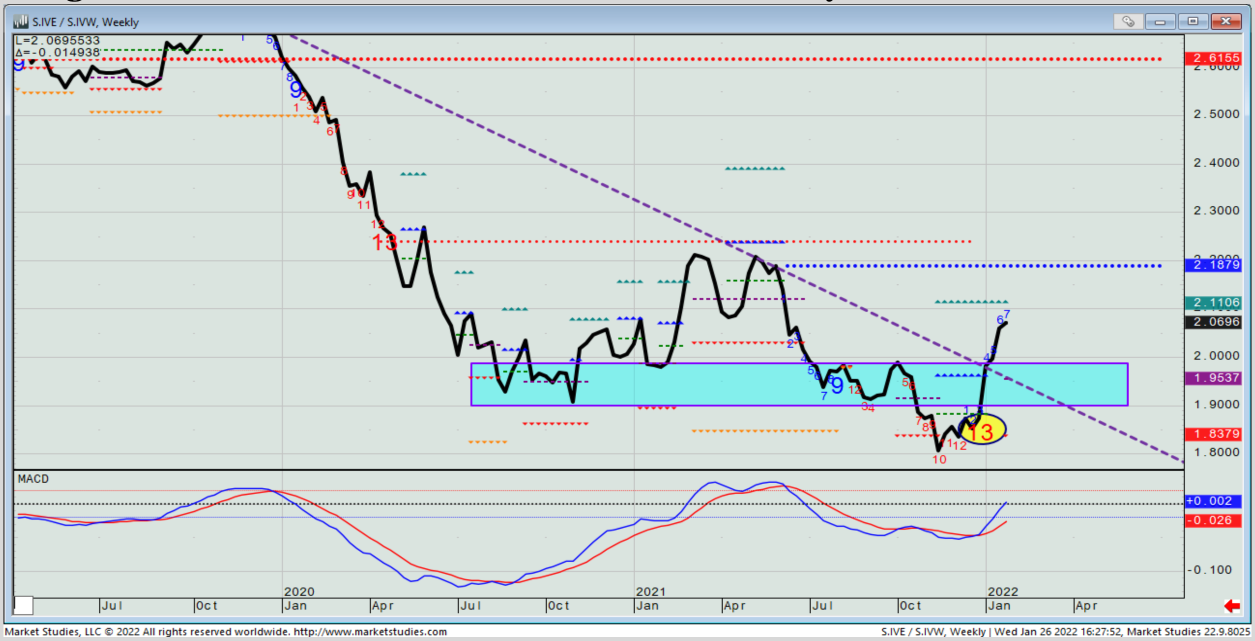
Other Open Recommendations and Positions

Long IVE (Value) vs. Short IVW (Growth)

We started to enter a position in this last Friday, putting on a ¼-unit of this pair (avg. price of 2.047) and were looking to add another 50% position within the highlighted box value (approx. 1.98 to 1.90), and the final 25% at 1.855 to 1.852. That's making a bet that the cyclical low is in place.

If this simply goes up without our adding any more, we'll get out on the Friday close in two more weeks if that week is on a Setup +9 count. We needn't concern ourselves with what would only be a 25%-sized position.

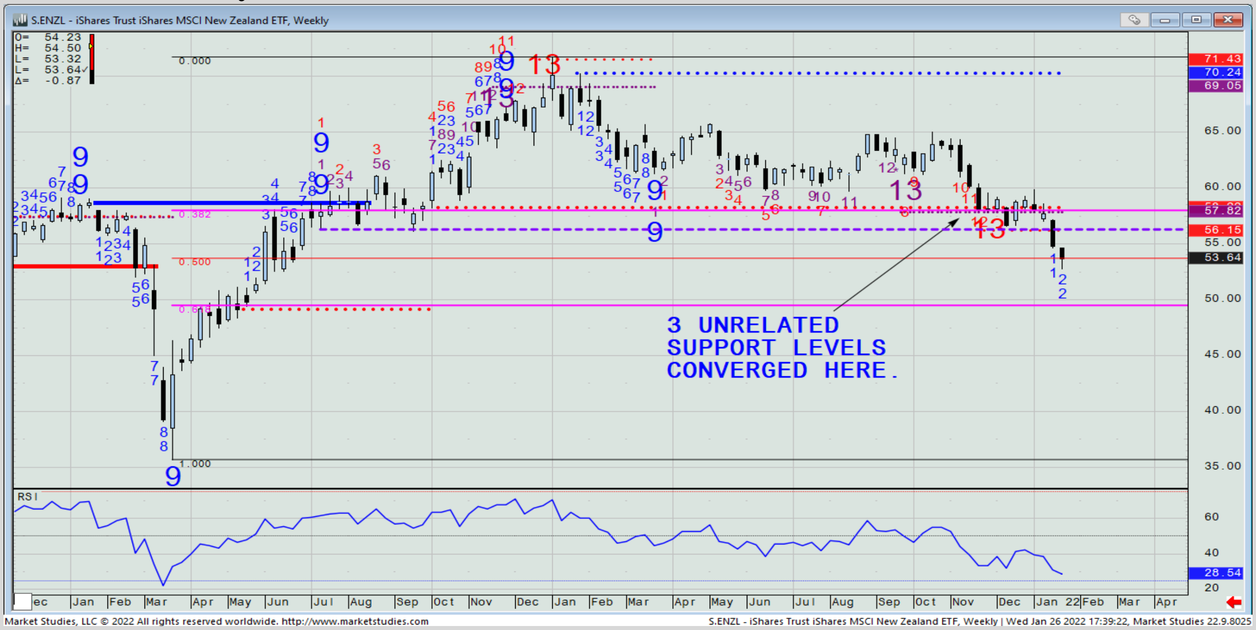
Long IVE (Value) vs. Short IVW (Growth) – Weekly



Long iShares MSCI New Zealand fund (ENZL)

We were long one-half unit (avg. price of $58.58), and added another half-unit at $58.74 and had a stop out on a Friday close < $56.29, the lowest low of the triple-bottom of Summer 2020 (i.e., the purple-colored dashed line). That happened last Friday so we exited at $54.78. We lost 6.6%.

ENZL – Weekly



Long SPDR Energy (XLE) vs. Short SPDR Industrials (XLI)

Almost seven weeks ago we got our entry into this pair trade by going long one unit of XLE and short one unit of XLI (avg. entry price of 0.5433). We just took half off at our first target of 0.65 +/- 0.0030, and we'll again raise our sell-stop to unwind the remaining half on consecutive *daily* closes < 0.6281.

Long XLE vs. Short XLI – Weekly

Suggestions and Explanation of Terms

With every major firm brokerage firm having gone to $0 domestic stock/ ETF commissions, you should not be paying anything to trade my recommendations (other than the associated fees to placing a short position we occasionally recommend).

Cloud Charts (a.k.a. "Ichimoku")
"Cloud" charting is a far-eastern technical model that was developed over 50 years ago, but is still not commonly used in the US (nor is there much reference material available on it, either). The calculations involved in the construction of each of the 5 lines that make up this model are simple math (see below). The proper understanding and use of cloud charts are still somewhat a mystery to many in the western world. We, however, have a deep understanding of this model, and use it as a core component to our market analysis.

The names and calculations of the 5 lines are as follows:

- Conversion Line: the arithmetic midpoint of the most recent 9 price bars (inclusive of the current bar).
- Base Line: the arithmetic midpoint of the most recent 26 price bars (inclusive of the current bar).
- Leading Span 1: the midpoint of the previously calculated Conversion and Base Lines, plotted forward 26 bars (including the current bar).
- Leading Span 2: the arithmetic midpoint of the most recent 52 price bars (including the current bar) plotted forward 26 bars (including the current bar).
- Lagging Span: the current price plotted backwards 26 bars (including the current bar).
- The "Cloud" is the area on the chart bounded by the two Leading Spans.

In any given timeframe, it is our interpretation of the relationship of a security's price to these five lines -- and the relative positions of these lines to each other -- that helps us decipher behavioral and/or structural shifts to the current bull or bear market environment at hand.

DeMark Studies (a.k.a. TD models)
DeMark Studies consist of models created by Tom DeMark, a noted market-timing indicator developer and consultant to many major Wall Street institutions. Two of these models that look for the timing of trend exhaustion include TD Sequential and TD Combo. A third, TD Propulsion, looks for a specific price exhaustion level after a trend momentum level has been properly identified and thrust through.

Some key phrases we use in our writings include:

- TD Setup: Nine consecutive price bars that the closing price is above the close from four bars prior (a.k.a. "Setup +9"). When completed and "perfected" (i.e. the 8th or 9th bar's high is higher than both bar 6's and 7's highs), a near-term **top** may be in place. Conversely, is a run of nine consecutive price bars that the closing price is beneath the close from four bars prior (a.k.a. "Setup -9"). When completed and "perfected" (i.e. the 8th or 9th bar's low is lower than both bar 6's and 7's lows, a near-term price **bottom** may be in place.
- TD Sequential: After a completed Setup +9 count, if the security continues to move higher by a certain amount, a full trend has developed. This model looks to identify the exhaustion point of that trend, from a timing perspective. Here's how: Subsequent to the Setup +9, the model then looks for 13 price bars (that needn't be consecutive) that the closing price is greater than the high from two price bars back. When this happens, odds have increased that first buying within the current uptrend is much riskier than normal; some choose to actually lighten long exposure, too. Some aggressive traders even choose to initiate short exposure. Conversely, after a Setup -9 count, the model then looks for 13 price bars (that needn't be consecutive) that the closing price is less than the low from two bars back. When this happens, odds have increased that first selling within the current downtrend is much riskier than normal; some choose to actually lighten short exposure, too. Some aggressive traders even choose to initiate long exposure. **Thus, some aggressive-style accounts often use this model to take profits or even enter new counter-trend positions.**
- TD Combo: This is a sister timing model to the above –mentioned Sequential model. It also reaches its trend exhaustion reading at a +13 or -13 reading. It counts to the 13th bar using a different calculation than Sequential. But it's potential implications for an impending trend reversal are the same.
- TD Propulsion: This model looks to define the initiation of a momentum move (whether higher or lower). Once the identified Propulsion Momentum level is properly surpassed, it then pinpoints measured exhaustion levels for that same breakout or breakdown move (i.e. Propulsion Exhaustion and Full Propulsion Exhaustion).
- TD Trend Factors: This model looks to define important support or resistance levels from previous highs or lows of moves, measured in increments of 5.56%. (This particular number is a derivative of the Fibonacci sequence of numbers.)

- "Qualified and Confirmed" Breakouts (**Updated**):

  To qualify and confirm an upside breakout of some level we reference, the following need occur, in order:
  1. A down close the price bar immediately before closing above the reference level
  2. The actual close above the reference level

3. A gap higher open; a higher daily high; and a higher daily close the next trading day.

To qualify and confirm a downside breach of some level we reference, the following need occur, in order:

1. An up close the price bar immediately before closing beneath the reference level
2. The close beneath the reference level
3. A gap lower open; a lower daily low; and a lower daily close the next trading day.

Thus, the qualified and confirmed process takes 3 consecutive price bars to create the signal.

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